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No. 73-890

IN THE

Supreme Court of the United States

OCTOBER TERM, 1973

ERIE LACKAWANNA RAILWAY COMPANY, Debtor,
Petitioner,

vs.

NORFOLK AND WESTERN RAILWAY COMPANY,
Respondent.

BRIEF OF NORFOLK AND WESTERN RAILWAY COMPANY IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

RICHARD J. FLYNN
1730 Pennsylvania Avenue
Washington, D.C. 20006

THEODORE N. MILLER
GEORGE L. SAUNDERS, JR.
HOWARD J. TRIENENS
One First National Plaza
Chicago, Illinois 60670

Counsel for Respondent

Of Counsel:

JOHN S. SHANNON
SIDLEY & AUSTIN
TAFT, STETTINIUS
& HOLLISTER

TWENTIETH CENTURY PRESS, CHICAGO 60605

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BRIEF OF NORFOLK AND WESTERN RAILWAY COMPANY IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

Norfolk and Western Railway Company respectfully submits this Brief in Opposition to the Petition for a Writ of Certiorari filed by the Erie Lackawanna Railway Company to review an order of the United States Court of Appeals for the Sixth Circuit entered on September 14, 1973.

JURISDICTION

The jurisdictional requisites are adequately set forth in the petition.

QUESTIONS PRESENTED

Petitioner has sought to raise questions which go far beyond the narrow issues decided by the Court of Appeals and which take no account of the nature of the federal income tax returns filed by petitioner and respondent fol-

lowing the Court of Appeals' decision. The questions actually presented in this case are:

1. Whether the Court of Appeals was correct in vacating an injunction which would have prevented the Norfolk and Western from filing its federal income tax return for the year 1972 in accordance with its rights and obligations under applicable provisions of the Internal Revenue Code and Income Tax Regulations.

2. Whether petitioner is entitled to or needs an injunction to restrain the Norfolk and Western from exercising its right to make elections in its consolidated tax return including the Erie for the year 1972, where the Erie Trustees had no interest in the Erie properties until June 26, 1972, and where the elections actually made in the Norfolk and Western's return were those urged by the Erie Trustees themselves for the period after that date.

STATUTES, REGULATIONS AND RULINGS INVOLVED

In addition to 11 U.S.C. Section 205 (Section 77(a) of the Bankruptcy Act), Section 1502 of the Internal Revenue Code of 1954, and Income Tax Regulations Section 1.1502-77, which appear in the Appendix to the Petition, Sections 1504(a) and (b) of the Internal Revenue Code of 1954, Section 1.1502-76(b)(1) of the Income Tax Regulations, and Revenue Ruling 63-104 appear in Appendix B hereto, *infra,* pp. B-1-B-4.

STATEMENT OF THE CASE

The Norfolk and Western Railway Company was compelled on April 1, 1968, to purchase 100% of the common stock of the Erie Lackawanna Railway Company under an order of the Interstate Commerce Commission which required the Norfolk and Western to exchange stock having a value of $55,026,000 for Erie stock. *Norfolk & Western Ry. Co. and New York, C. & St.L.R.Co. Merger,* 330 I.C.C. 780(1967). At the time of this acquisition, the Erie was in grave financial difficulty as a result of substantial losses

which it had suffered in the years prior to the acquisition and its prospects for continuing losses in future years. Notwithstanding its financial condition, the Erie contended in the proceedings before the Commission that the Norfolk and Western could fairly be compelled to acquire its stock at that price because of the tax advantages the Norfolk and Western would realize from inclusion of the Erie in a consolidated tax return and the use by the Norfolk and Western in that return of accelerated depreciation and other elections available under the Internal Revenue Code (JA 42-43;[1] Erie Reply Brief, ICC Docket No. 21510, Oct. 19, 1966, pp. 36-37):

> ". . . N&W could use EL's [Erie-Lackawanna's] investment credit and in addition obtain a tax deduction of at least $10.2 million per year by putting New EL on guidelines and accelerated depreciation . . . .
>
> "Because of those very real tax benefits, N&W is therefore certain to recover its investment in EL."

The Commission accepted this contention and, in reliance upon the tax savings which would be available after the acquisition, ordered the Norfolk and Western to pay the Erie the price it proposed (330 I.C.C. at 846):

> "Even if EL earnings are not sufficient to support the proposed stock exchange ratios, N&W's investment in EL would be protected by [the] substantial tax benefits [described in the EL testimony]."

The Commission's inclusion order was upheld by the United States District Court for the Southern District of New York on the basis of these same tax advantages. (*Erie Lackawanna R. Co.* v. *United States,* 279 F. Supp 316, 346 (1967)):

> "The Commission also correctly noted that 'even if E-L earnings are not sufficient to support the proposed

[1] The Joint Appendix in the Court of Appeals is referred to herein as "JA-. . . ."

> stock exchange ratios, N&W's investment is protected since E-L's income would be earned subject to five substantial tax benefits,' including several not heretofore mentioned. 330 I.C.C. 816 and 846-47. E-L's brief contains computations not challenged by N&W showing that tax savings will insure N&W's recovery of its $55 million investment in E-L within 10 years even if E-L earned nothing. In the light of all this, the Commission was justified in concluding that any overestimate of E-L's earning power was fully compensated, 330 I.C.C. at 816."

This Court affirmed the district court's decision and its findings of fact on this point. *Penn-Central Merger Cases,* 389 U.S. 486, 525-526 (1968).

Following its forced acquisition of the Erie, the Norfolk and Western filed consolidated tax returns in precisely the manner contemplated by the Commission's order. The Erie continued to suffer substantial losses which, when taken into the Norfolk and Western's consolidated return along with some of Erie's investment credits, produced substantial tax savings for the Norfolk and Western. However, the Norfolk and Western had not recouped even one-half of its investment in the Erie through such savings at the time this litigation was commenced (JA-5[illegible]).

The losses suffered by the Erie eventually forced it to file a petition for reorganization on June 26, 1972. The filing of this petition did not break the affiliation for tax purposes between the Norfolk and Western and the Erie under the applicable provisions of the Internal Revenue Code and Income Tax Regulations, nor did it relieve the Norfolk and Western of its obligation to include the Erie in its consolidated return. Nonetheless, in 1973, when the Norfolk and Western was preparing its 1972 return on a consolidated basis as required by the Income Tax Regulations, the Erie Trustees demanded that the tax benefits resulting from the Erie's inclusion in the consolidated

return be turned over to them. When the Norfolk and Western refused, the Trustees filed an application in the reorganization court on August 3, 1973, seeking, among other things, to enjoin the Norfolk and Western from including the tax attributes of the Erie in its 1972 consolidated return during the period after June 26, 1972, or, alternatively, to require the Norfolk and Western to report the operations of the Erie after that date on the basis specified by the Trustees. The application also sought compensation for all tax attributes of the Erie used by the Norfolk and Western since its forced acquisition and for any of those attributes that may be used in the future.

On the day the Trustees' application was filed, the district court issued a temporary order without notice restraining the Norfolk and Western from including the Erie in its 1972 consolidated income tax return for the period after the filing of the reorganization petition. Subsequently, in a decision handed down on September 10, 1973, the district court held that it need not resolve the question of whether the Erie could properly be included in the Norfolk and Western's consolidated return for the period after the filing of the petition for reorganization (A1, A11).[2] It permitted the Norfolk and Western to file a consolidated return including the Erie for 1972 but authorized and directed the Trustees to file a separate return for the Erie alone covering the period from June 27 through December 31, 1972—the portion of that year during which the Erie was in reorganization—thus leaving it to the Internal Revenue Service and reviewing courts to determine which return was correct for that period (A12). However, with respect to its consolidated return for the entire tax year, the district court went on to enjoin the Norfolk and Western (*id.*):

> ". . . from exercising or making any and all tax elections and from taking any and all deductions and

[2] The opinion of the district court and the opinion of the Court of Appeals are reproduced in the Appendix to the Petition, which is referred to herein as "A . . . ."

> credits which are available to the Debtor in the computation of its separate taxable income under the Internal Revenue Code and the regulations thereunder, except such tax elections, deductions, and credits as the Trustees, subject to the control of this Court, shall determine."

The district court expressly refused to find that this injunction was necessary to prevent acts that would "unduly hinder, delay, burden, interfere, or be inconsistent with the pending corporate reorganization" (A11). It did make a conclusory finding that the injunction was necessary to protect the Erie from irreparable injury (A11), but it nowhere explained how such injury could possibly flow from the filing of a return by the Norfolk and Western that would not and could not have any binding effect upon the Erie, since the Erie was filing its own separate return.

The Court of Appeals for the Sixth Circuit reversed the district court's decision on September 14, 1973 (A14). The Court of Appeals found that the Erie was not faced with irreparable injury from the filing by the Norfolk and Western of a consolidated tax return including the Erie, but, indeed, that the Erie has "an adequate remedy at law" for every claim that it asserted (A17). The Court of Appeals also pointed out that there are established administrative procedures for reviewing income tax returns filed by taxpayers and held that it was premature at this point for the district court to decide whether the Erie's tax attributes are property, and, if so, who owns that property (A16-17).

Following the Court of Appeals' decision, the Norfolk and Western proceeded to complete and file its 1972 income tax return. In doing so, the Norfolk and Western made its elections under the Internal Revenue Code with respect to the operations of the Erie so as to minimize, to the fullest extent permitted by law, the depreciation attributed to the assets of the Erie for the period following the date

of the filing of the petition for reorganization. A copy of that return was furnished to the Erie Trustees, who were specifically informed of the basis upon which it had been prepared. (See letter attached hereto as Appendix A, p. A-1, *infra.*)

The Norfolk and Western's 1972 return was filed on September 17, 1972, as required by law. The Erie Trustees also filed a return as had been directed by the district court. Since the Norfolk and Western's return minimized the depreciation attributed to the assets of the Erie, the effect of the Trustees' return upon the basis of those assets could not differ from that of the return filed by the Norfolk and Western for the period following the date of the filing of the petition for reorganization.

ARGUMENT

The petition for certiorari should be denied because, as will be shown below, it fails to meet any of this Court's standards governing the granting of such petitions. Moreover, as will also be shown, the petition should be denied because this case, in its present posture, does not actually present any substantial question which is appropriate for resolution by this Court.

I. THE COURT OF APPEALS WAS CORRECT IN VACATING THE INJUNCTION OF THE DISTRICT COURT.

As the Court of Appeals pointed out, both the structure and the purpose of the Internal Revenue Code and Regulations and Rulings promulgated thereunder flatly preclude the issuance of an injunction, either prohibiting a taxpayer from filing a consolidated return including all members of the affiliated group, as sought by the Trustees in the district court, or requiring that the return be prepared on a specified basis, as ordered by the district court and contended for by the Trustees here. An income tax return is strictly

a matter between the taxpayer filing that return and the Government. The sole purpose of the return is to state the taxpayer's position with respect to the taxes it owes the Government in accordance with applicable revenue laws. The filing of a return does not therefore affect the substantive rights of another party, either against the Government or against the taxpayer that prepared the return.

The Code and Regulations prescribe the method by which returns are to be prepared and filed by each taxpayer. Here the Code and Regulations make it plain that the Norfolk and Western not only is authorized, but is required, to file a consolidated return including the Erie for the entire tax year 1972. The Court of Appeals found (A16):

> "Under applicable statutes and regulations N&W has been filing consolidated income tax returns since 1954. Upon its forced acquisition of all the common capital shares of Erie in 1968, N&W has since included in its consolidated tax return the income or losses and other tax attributes of Erie. It cannot now change without the consent of the Commissioner of Internal Revenue, who will undoubtedly audit these returns."[3]

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[3] The obligation of the Norfolk and Western to include the Erie in its 1972 consolidated return arises from the provisions of sections 1504(a) and (b) of the Internal Revenue Code of 1954, Income Tax Regulations sections 1.1502-76(b)(1) and the fact that the Norfolk and Western has filed consolidated returns including the Erie in previous years. The fact that the Erie is now in reorganization proceedings does not affect this obligation of the Norfolk and Western. Revenue Ruling 63-104 provides (1963-1 Cum. Bull. 172):

> "An affiliated group of corporations, which has filed consolidated returns for prior taxable years, is required to file a consolidated return for a subsequent taxable year in which none of the exceptions provided in section 1.1502-11(a) [the predecessor to the currently effective section 1.1502-75(c)] of the Income Tax Regulations is applicable, even though a member of the group is involved in bankruptcy proceedings and the trustee in bankruptcy fails or refuses to file a Form 1122 consenting to the filing of such a return."

Petitioner has challenged this interpretation of the applicable provisions of the Internal Revenue Code and Income Tax Regulations by filing a separate return for a part of the tax year 1972.[4] By this filing, it placed all questions of the correctness both of its return and of the return filed by the Norfolk and Western squarely before the responsible federal administrative authorities which process such returns. However, petitioner is not content to let these authorities resolve those questions. Instead, it has asked this Court to substitute itself as the initial arbiter of the obligations of the Norfolk and Western and the Erie, as taxpayers, to the Government.

There is no legal basis whatever for such a resort to the courts for what amounts to a declaratory judgment as to the meaning of the Internal Revenue Code.[5] Petitioner has not cited—and our research has failed to disclose—a single case in which the obligation of a parent to include an affiliated subsidiary in its consolidated return has been nullified or controlled in any way by judicial decree prior to a determination by the taxing authorities. Indeed, we have been unable to find a single case prior to this one in which an injunction has been sought to prevent a taxpayer from filing its tax return on whatever basis it saw fit.

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[4] The Trustees did not ask and consequently were not granted permission to file a separate return for the part of 1972 preceding the filing of the petition for reorganization. Of course, if they had any legitimate doubt as to the correctness of the Norfolk and Western's return for that period, they should have requested the right to file a separate return for the period.

[5] 28 U.S.C. § 2201 forbids the federal courts from granting declaratory judgments in cases involving federal taxes. See *In re Statmaster Corp.*, 465 F.2d 978 (5th Cir. 1972); *Jolles Foundation* v. *Moysey*, 250 F.2d 166 (2nd Cir. 1957); *In re Inland Gas Corp.*, 241 F.2d 374 (6th Cir.), *cert. denied*, 355 U.S. 838 (1957); *Wilson* v. *Wilson*, 141 F.2d 599 (4th Cir. 1944).

The purpose of an income tax return, the clear requirements of the Internal Revenue Code, Regulations and Rulings, and the total absence of precedent to justify an injunction such as that sought by the Trustees led the Court of Appeals to conclude that the injunction issued by the district court should be vacated so that the entire matter can be left in the hands of the taxing authorities where it belongs. We submit that this decision was clearly correct.

Petitioner does not challenge, or indeed even mention, these clear provisions of the Internal Revenue Code and Income Tax Regulations or the established procedures by which tax controversies are resolved. Instead, it challenges the Court of Appeals' decision, and hence the Norfolk and Western's right even to present its position to the responsible taxing authorities, on the theory that all tax attributes arising from the operations of the Erie are "property" of the Erie which passed into the hands of the Erie Trustees upon the filing of its petition for reorganization. The short answer to this contention is that it is patently premature. As the Court of Appeals pointed out, the issue of whether the tax attributes of the Erie are property in the hands of the Erie Trustees may be rendered moot by the administrative proceedings which regularly follow the filing of income tax returns. The Court of Appeals did not attempt to anticipate or predict the outcome of the taxing authorities' proceedings. Instead, it held that the district court should await the outcome of such administrative proceedings before deciding a question that may become moot (A17):

> "Thus, the question of whether the past, present or future tax attributes belong to Erie or N&W can later be determined by the District Court in the event that

such issues are not adjudicated administratively by the Commissioner, the Tax Court or on appeal to a United States Court of Appeals."

This approach is clearly correct and consistent with the established principle that courts should not reach out to decide questions that may not have to be decided. This principle has been recognized in many cases decided by this Court. See, e.g., *Sanks* v. *Georgia,* 401 U.S. 144 (1971); *United States* v. *Fruehauf,* 365 U.S. 146 (1961); *Barr* v. *Mateo,* 355 U.S. 171 (1957); *Eccles* v. *Peoples Bank,* 333 U.S. 426, 432 (1948). It is particularly applicable here, where the question unnecessarily pressed involves a legal question which both the district court and the Erie Trustees recognize is one of first impression (JA-131; Petition, p. 10), and a fact situation that is unique.

There can be no justification for reaching out to decide an issue of this nature here, since it is clear, and indeed undisputed, the petitioner will suffer no loss from awaiting the determination of the correctness of its return and the Norfolk and Western's return by the responsible taxing authorities. Nothing that the Internal Revenue Service does or does not do with respect to the Norfolk and Western's return will affect the rights of the Erie with respect to its own returns. When and if the Erie earns income on which it would otherwise be obligated to pay taxes, the Erie will be entitled to assert any rights it may have to offset that income with losses carried over from its own return. The question of its tax liability will not be governed by any resolution that may have been made with respect to the Norfolk and Western's tax liability. Thus, as the Court of Appeals pointed out, "the Trustees have an adequate remedy at law" (A17), even if they are right on the sub-

stantive issues involved.[6] Petitioner in no way challenges this finding, which conclusively establishes that the issuance of the injunction by the district court was improper, and that the Court of Appeals was correct in vacating that injunction and deferring decision on the property issue.

II. THE FILING BY THE NORFOLK AND WESTERN OF A CONSOLIDATED RETURN, INCLUDING THE ERIE, FOR THE ENTIRE YEAR 1972 HAS NOT ERODED THE BASIS OF THE ASSETS OF THE BANKRUPT ESTATE.

The injunction of the district court having been vacated, the Norfolk and Western had a clear right, both under the Internal Revenue Code and Regulations and under the *Inclusion* order, to file its 1972 tax return in any manner it saw fit consistent with law, including the right to make any elections available to it under the Code and Regulations. However, as already pointed out, the Norfolk and Western prepared its 1972 return for the period following June 26, 1972, so as to minimize, to the full extent permitted by law, the depreciation attributable to the assets of the Erie. Petitioner has not identified any substantial difference between the return filed by the Norfolk and

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[6] The Norfolk and Western believes, and argued strongly in the Court of Appeals, that the Erie's tax losses are not property which passed to the Erie Trustees. Loss carryovers have no intrinsic value or legal status; their significance is created and wholly governed by the Internal Revenue Code, which requires the Norfolk and Western, in this case, to include the Erie's losses in its consolidated return. As pointed out below, (p. 16, *infra*), this Court has not decided, but, indeed, has expressly reserved the question of whether tax loss carryovers can ever properly be treated as property within the meaning of the Bankruptcy Act. As the Court of Appeals pointed out, this is an inappropriate case in which to resolve that question, since it may prove to be totally unnecessary. Moreover,

Western for this period and the separate return filed for the Erie by its Trustees at the direction of the district court.

Thus, petitioner's efforts to create the impression that the Norfolk and Western is eroding the tax basis of the assets of the bankrupt estate by elections it has chosen to make under the Internal Revenue Code are not sound. In view of the nature of the return filed by the Norfolk and Western, the only question of any practical significance presented at this stage of the case is whether the Erie Trustees have a right to control the Norfolk and Western's elections during the period *before* the filing of the petition for reorganization. We submit that it is clear that the Trustees have no legal basis for objecting to the Norfolk and Western's elections during this period—before they had any interest in the Erie. As shown above, the suggestion for placing the Erie on the tax basis chosen by the Norfolk and Western originated with the Erie itself as a justification for the price it compelled the Norfolk and Western to pay for its stock in the inclusion proceedings. The Interstate Commerce Commission expressly adopted this suggestion and ordered

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the circumstances under which the Norfolk and Western was compelled to acquire the Erie at a price which expressly took into account the benefit of the Erie's tax attributes, coupled with the fact that the Norfolk and Western has not now and will not for some time in the future recover its investment through use of these tax attributes, are also significant. These facts create a situation in which, even if the tax attributes of the Erie are regarded as property, such property belongs not to the Erie Trustees, but to the Norfolk and Western. The Court of Appeals also reserved this issue (A16-17). Since there is no precedent directly in point with respect to either of the issues reserved by the Court of Appeals, that court was clearly correct in holding that such novel, legal and factual questions should not be decided at this stage of the proceedings.

the inclusion at the proposed price on that basis. The *Inclusion* order was affirmed by the courts on the same basis. In these circumstances, the Norfolk and Western's elections with respect to the Erie prior to the date of the filing of the petition for reorganization were the direct product of the *Inclusion* order.

Petitioner's efforts to justify a legitimate interest in the Trustees in pre-reorganization tax attributes on the basis of Justice Jackson's dissent in *Western Pacific R. Corp.* v. *Western Pacific R. Co.*, 345 U.S. 247 (1953), and on *In re Bob Richards Chrysler-Plymouth Corp., Inc.*, 473 F.2d 262 (9th Cir.), *cert. denied*, 412 U.S. 919 (1973), and *Case* v. *New York Central R. Co.*, 15 N.Y.2d 150, 204 N.E.2d 643 (N.Y. Ct. App. 1965), are unfounded. Contrary to the implication in the petition (pp. 7-8), the portion of the Court of Appeals' decision in *Western Pacific* which this Court refused to review held that a company suffering a loss does not have an interest in that loss of a nature that would justify a court in compelling an affiliated company with income to pay for the tax benefits realized from using that loss (197 F.2d 994, 1004 (9th Cir. 1951)):

> "There is nothing in the Code or Regulations that compels the conclusion that a tax saving must or should inure to the benefit of . . . the company which has sustained the loss that makes possible the tax saving."

The *New York Central* case is to the same effect in that it held that courts will not impose obligations upon companies affiliated for tax purposes or modify agreements between them. *In re Bob Richards Chrysler-Plymouth* held only that a parent was not entitled to retain as a set-off a tax refund resulting from the carryback of a bankrupt subsidiary's net operating loss during the year of bankruptcy to reduce taxable income of the same subsidiary during

preceding years and with respect to which the subsidiary had paid tax. The Erie has had no taxable income and has paid no income tax since it was acquired by the Norfolk and Western. In any event, none of these cases involved the forced acquisition of a subsidiary and its tax attributes.

Petitioner's arguments that the Norfolk and Western has usurped the powers of the Trustees and somehow eroded the estate which passed into their hands thus really comes down to an effort to make this Court an "umpire to debates concerning harmless, empty shadows." *Poe* v. *Ullman*, 367 U.S. 497, 508 (1961). The Trustees had no legal interest in the Erie prior to the filing of the petition for reorganization, and nothing done by the Norfolk and Western during that period could remotely be characterized as illegal or improper. The Trustees themselves recognized this fact in requesting and obtaining from the district court permission to file a separate return only for the period after the filing of the petition for reorganization—June 27, 1972 through December 31, 1972 (A12). Moreover, for the entire period since the date of the filing for reorganization, the Trustees' wishes have been fully complied with. There is simply no genuine dispute for this Court to resolve with respect to the erosion of the bankrupt estate.

III. THERE IS NO CONFLICT AMONG THE CIRCUITS ON ANY QUESTION INVOLVED IN THIS CASE.

Petitioner's effort to demonstrate a conflict among the circuits on the question of whether the tax attributes of the Erie are property of the Trustees is patently unpersuasive. Not a single one of the cases cited by petitioner deals with the question of whether tax attributes, such as losses or depreciation, are property within the meaning of the Bankruptcy Act. Instead, most of the cases cited deal with the question of whether a tax refund to a wage earner resulting

from excess withholding of income tax from his pre-bankruptcy wages, but paid to him after the commencement of the bankruptcy proceedings, constitutes property passing to the trustee pursuant to the Bankruptcy Act.[7] The only other case cited, *In re Aveni*, 458 F.2d 972 (6th Cir.), *cert. denied*, 409 U.S. 877 (1972), is equally inapposite since it involved only the question of whether unpaid wages which had accrued to the bankrupt when the bankruptcy petition was filed were property passing to the trustee.

In *Segal* v. *Rochelle*, 382 U.S. 375 (1966), this Court held that inchoate claims for *refunds* resulting from a loss carryback are property within the meaning of the Bankruptcy Act, but expressly reserved the question of whether loss carryovers could properly be held to have that status (*id.*, at 381):

> "We are told that if this loss-carryback refund claim is 'property,' that label must also attach to loss-carryovers, that is, the application of pre-bankruptcy losses to earnings in future years. Since losses may be carried forward five years and in some cases even seven or ten years, I.R.C. §§ 172(b)(1)(B)-(D), great hardship for the estate is foreseen by petitioners in keeping it open for this length of time. While in fact the trustee can obviate this detriment to the estate—by selling a contingent claim in some instances or simply foregoing it—inconvenience and hindrance might be caused for the bankrupt individual. Without ruling in any way on a question not before us, it is enough to say that a carry-

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[7] *Compare, In re Kingswood*, 470 F.2d 996 (9th Cir. 1972), *rev'g* 343 F. Supp. 498 (C.D. Cal. 1972), *In re Cedor*, 337 F. Supp. 1103 (N.D. Cal.), *aff'd per curiam*, 470 F.2d 996 (9th Cir. 1972), *cert. denied*, 411 U.S. 973 (1973), *with, In re Kokoszka*, 479 F.2d 990 (2nd Cir. 1973), *In re Jones*, 337 F. Supp. 620 (D. Minn. 1971), *leave to appeal denied* (8th Cir. May 14, 1971), *cert. denied*, 404 U.S. 1040 (1972).

over into post-bankruptcy years can be distinguished conceptually as well as practically."[8]

There clearly is not a conflict on the question reserved in *Segal*. Indeed, the fact of the matter is that no Court of Appeals, including the Court of Appeals which decided this case, has passed upon that question. Nor is there any other reason for the Court to consider that question in this case.

IV. REVIEW OF THIS CASE IS NOT JUSTIFIED ON GROUNDS OF THE IMPORTANCE OF THE ISSUE INVOLVED OR ITS IMPACT UPON THE NORTHEASTERN RAILROADS.

Petitioner also seeks to justify review on the ground that the right of the Norfolk and Western to make elections with respect to a bankrupt subsidiary is an important issue in the administration of the Bankruptcy Act, and that the question of whether tax attributes are property has an important impact upon the Northeastern railroads. Neither of these contentions is sound.

We have already shown that the Norfolk and Western did not make elections of the nature complained of by the

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[8] There is an obvious difference, recognized by this Court in making the distinction in *Segal*, between a loss carryback *refund* where the income, as well as the offsetting loss, is earned by the bankrupt prior to the filing of the bankruptcy petition, and a loss *carryover* which may reduce tax liability, if at all, only when pre-bankruptcy losses of the bankrupt are utilized to reduce post-bankruptcy taxable income. As pointed out in Collier's basic treatise on Bankruptcy (4A Collier on Bankruptcy ¶ 70.28):

"The loss-carryforward claim seems much more replete with problems of an equitable nature and of a practical nature than the loss-carryback claim. It is clear that the Court has not answered the question at all except to the effect that the two situations are completely different."

petitioner with respect to the period following the filing of the petition for reorganization. Hence, this case poses no question of the kind characterized as novel and important by the petitioner.

The claim that the property question sought to be raised will have an important impact on the Northeastern railroads is equally unsupportable. The situation presented in this case is one that is unique among all of the bankrupt railroads in the Northeast, since the Erie is the only one of those railroads which is owned by a company which was compelled to buy it on the grounds of the tax advantages available. The issues raised in cases involving other Northeastern railroads are entirely different.[9]

Petitioner has also sought to create the impression that the questions presented here are "crucial" to the Erie's prospects of being reorganized as a viable, profitable railroad. This claim is flatly inconsistent with the findings of the district court, which expressly refused to find that its injunction was necessary to prevent any action which "could

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[9] The case cited involving the Lehigh Valley Railroad Company (E.D. Pa. Bankruptcy No. 70-432) is totally different from the question sought to be presented here. As the petition itself concedes (p. 11), the bankrupt railroad there is merely seeking permission to file a separate return, in addition to the consolidated return including it filed by its parent. The Erie trustees have already filed such a return with the permission of the bankruptcy court.

The controversy cited involving the Boston and Maine Railroad is fundamentally different from the situation here in that the Boston and Maine controversy does not involve the forced acquisition of an unprofitable railroad with the purchase price justified on the basis of tax savings to the acquiring corporation. Hence, it is clear that the resolution of whether the Erie's tax attributes are property passing to the trustee is not dispositive of whether the trustees of the Boston and Maine can compel compensation for use of their losses.

unduly hinder, delay, burden, interfere, or be inconsistent with the pending corporate reorganization" (A 11). Petitioner seeks to obviate this finding by reference to the Regional Rail Reorganization Act of 1973, which became law on January 2, 1974, Pub. L. No. 93-236. However, this law contains no provisions which would make the issue sought to be presented here any more important to the reorganization of the Erie than that issue would be under Section 77 of the Bankruptcy Act.

The district court's refusal to premise its injunction on the necessity of preventing an action which would frustrate the reorganization of the Erie under Section 77 of the Bankruptcy Act confirms the abstract nature of the questions sought to be presented to this Court. In these circumstances the Court of Appeals was correct in concluding that the Erie is faced with no irreparable injury by the return filed by the Norfolk and Western and that further judicial proceedings should be deferred until injury is incurred and administrative proceedings exhausted.

CONCLUSION

For the foregoing reasons, respondent requests that the petition for writ of certiorari be denied.

Respectfully submitted,

RICHARD J. FLYNN
1730 Pennsylvania Avenue
Washington, D.C. 20006

THEODORE N. MILLER
GEORGE L. SAUNDERS, JR.
HOWARD J. TRIENENS
One First National Plaza
Chicago, Illinois 60670

Counsel for Respondent

Of Counsel:

JOHN S. SHANNON
SIDLEY & AUSTIN
TAFT, STETTINIUS
& HOLLISTER

January, 1974

APPENDIX A

September 17, 1973

Messrs. Ralph S. Tyler, Jr.,
and Thomas F. Patton
Trustees
Erie Lackawanna Railway Company
Midland Building
Cleveland, Ohio 44115

Dear Sirs:

The United States Court of Appeals for the Sixth Circuit having vacated the order of the District Court, Norfolk and Western has today filed its consolidated federal income tax return for the calendar year 1972 by including Erie Lackawanna for the full year.

For your information, this return reflects an annual depreciation allowance for Erie Lackawanna property of about $17.6 million. This depreciation was calculated on the basis of maximized deductions up to June 26, 1972, and minimized deductions thereafter. It compares with depreciation of about $24.6 million following procedures used in prior years.

Mr. Kiley will furnish Mr. Keenan with a copy of this return.

Sincerely,

/s/ John P. Fishwick

APPENDIX B

INTERNAL REVENUE CODE OF 1954, 26 U.S.C.

Sec. 1504. Definitions.

(a) DEFINITION OF "AFFILIATED GROUP".—As used in this chapter, the term "affiliated group" means one or more chains of includible corporations connected through stock ownership with a common parent corporation which is an includible corporation if—

(1) Stock possessing at least 80 percent of the voting power of all classes of stock and at least 80 percent of each class of the nonvoting stock of each of the includible corporations (except the common parent corporation) is owned directly by one or more of the other includible corporations; and

(2) The common parent corporation owns directly stock possessing at least 80 percent of the voting power of all classes of stock and at least 80 percent of each class of the nonvoting stock of at least one of the other includible corporations.

As used in this subsection, the term "stock" does not include nonvoting stock which is limited and preferred as to dividends.

(b) DEFINITION OF "INCLUDIBLE CORPORATION".—As used in this chapter, the term "includible corporation" means any corporation except—

(1) Corporations exempt from taxation under section 501.

(2) Insurance companies subject to taxation under section 802 or 821.

(3) Foreign corporations.

(4) Corporations entitled to the benefits of section 931, by reason of receiving a large percentage of their income from sources within possessions of the United States.

(5) Corporations organized under the China Trade Act, 1922.

(6) Regulated investment companies and real estate investment trusts subject to tax under subchapter M of chapter 1.

(7) A DISC or former DISC (as defined in section 9926).

INCOME TAX REGULATIONS, 26 CFR

Sec. 1.1502-76. Taxable Year of Members of Group.

* * * * *

(b) *Income to be included in returns for taxable year* —(1) *Inclusion of income in consolidated return.* The consolidated return of a group must include the income of the common parent for that corporation's entire taxable year (excluding any portion of such taxable year for which its income is properly included in the consolidated return of another group) and, except as provided in subparagraph (5) of this paragraph, the income of each subsidiary for the portion of such taxable year during which it was a member of the group. If § 1.1502-75(d)(2)(ii) applies to a group, then for purposes of this paragraph, the former common parent shall be deemed to continue in existence and shall be regarded as the common parent for the entire taxable year in which the acquisition occurs. If § 1.1502-75 (d)(3)(v) applies to a group, then for purposes of the application of this paragraph (other than to a group which ceases to exist as a result of the application of § 1.1502-75 (d)(3)(i)), the second corporation (whether or not it remains in existence) shall be treated as the common parent for the entire taxable year of such corporation in which the

acquisition occurs, and the first corporation shall be treated as a subsidiary for the portion of such taxable year subsequent to the acquisition.

REVENUE RULING 63-104, 1963-1 CUM. BULL. 172 (1963)

Advice has been requested whether, under the circumstances described, an affiliated group of corporations is required to make a consolidated return.

An affiliated group of corporations made consolidated returns for several years prior to the year in which a member of the group filed a voluntary petition in bankruptcy and was adjudicated a bankrupt. The trustee in bankruptcy failed to file a consent on Form 1122, Return of Information and Authorization and Consent of Subsidiary Corporation Included in a U.S. Consolidated Income Tax Return, to authorize the parent corporation to make a consolidated return on its behalf.

Section 1.1502-11(a) of the Income Tax Regulations provides, with certain exceptions not here pertinent, that, if a consolidated return is made for any taxable year, a consolidated return must be made for each subsequent taxable year during which the affiliated group remains in existence.

Section 1.1502-12(b) of the regulations provides, in pertinent part, that each subsidiary must prepare duplicate originals on Form 1122, consenting to the regulations under section 1502 of the Internal Revenue Code of 1954 and authorizing the common parent corporation to make a consolidated return on its behalf for the taxable year and authorizing the common parent (or, in the event of its failure, the Commissioner of Internal Revenue or the district director) to make a consolidated return on its behalf (as long as it remains a member of the affiliated group), for each year thereafter for which, under section 1.1502-11(a)

of the regulations, the making of a consolidated return is required.

Section 1.1502-12(d) of the regulations states that each return or form required to be made or prepared by a corporation must be executed by the person authorized under section 6062 of the Code to execute returns of separate corporations. In cases where a receiver or a trustee in bankruptcy is operating the property or business of a corporation, each return or form required to be made or prepared by such corporation must be executed by the receiver or trustee, as the case may be, pursuant to an order or instruction of the court, and be accompanied by a copy of such order or instructions.

Section 1.1502-18(a) of the regulations provides, in part, that, if there has been a failure to file any of the forms required by these regulations, notice thereof shall be given the common parent corporation by the Commissioner, and the tax liability of each member of the affiliated group shall be determined on the basis of separate returns unless such income is included or such forms are filed within the period prescribed in such notice, or any extension thereof, or unless under section 1.1502-11(a) of the regulations a consolidated return is required for such year.

Since section 1.1502-11(a) of the regulations makes no exceptions in the event of the bankruptcy of a member corporation, it is concluded that the general rule provided in that section is applicable even after a member corporation is adjudicated a bankrupt, unless one of the specific exceptions is applicable. This is consistent with the general rule that bankrupt corporations are treated the same as other corporations. See G.C.M. 12207, C.B. XII-2, 83 (1933).

Accordingly, assuming that none of the exceptions specifically provided in section 1.1502-11(a) of the regulations is applicable, it is held that the affiliated group is required to make a consolidated return.